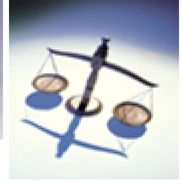
The Weekly Update of Texas Insurance News

TEXAS INSURANCE LAW NEWSBRIEF



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A Service of Martin, Disiere, Jefferson & Wisdom L.L.P.

Principal Office 808 Travis, Suite 1800 Houston, Texas 77002 713.632.1700 FAX 713.222.0101
111 Congress Avenue, Suite 1070 Austin, Texas 78701 512.610.4400 FAX 512.610.4401
900 Jackson Street, Suite 710 Dallas, Texas 75202 214.420.5500 FAX 214.420.5501

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FIFTH CIRCUIT INTERPRETS FIRST-PARTY PROPERTY DEDUCTIBLE CLAUSE

In *Texas Industries, Inc. v. Factory Mutual Insurance Company*, 2007 WL 1376337 (May 11, 2007), the Fifth Circuit Court of Appeals had the opportunity last week to interpret a "15 Day's Value Time Element of the Objects Experiencing the Loss or Damage" Deductible Clause. In *Texas Industries*, TXI had started a previously-planned maintenance outage on Kiln No. 5 on January 5, 2003, which was to last until January 16, 2003. On January 7th, a fire damaged Kiln No. 5, but had no effect on the other kilns. As a result of this fire, production was interrupted until January 30th, and full production did not resume until February 3rd. There was a 23-day period in which Kiln No. 5 did not operate at all and a 4-day period in which partial operation occurred. Ten of the days without any operation were part of the previously-planned outage.

TXI submitted a business interruption insurance claim for its loss. The parties stipulated that the total business interruption loss actually sustained by TXI was $3,916,905. Under the policy, the deductible is to be subtracted from the amount of loss suffered in order to determine the amount of insurance proceeds to which TXI may be entitled. The proper calculation of the deductible was the sole issue before the Fifth Circuit.

First, the Court examined the express terms of the policy's deductible clause, the "15 Day's Value Time Element of the Objects Experiencing the Loss or Damage." Noting that the term in dispute was the "Day's Value Time Element of the Objects Experiencing the Loss or Damage," the Court then reviewed the policy's definition of this term. Next, the Court observed that the parties did not dispute that Kiln No. 5 was the only object which experienced a loss – there were no objects dependent on Kiln No. 5. The parties did, however, differ on their methodology of calculating the deductible under the "15 Day's Value Time Element of the Objects Experiencing the Loss or Damage."

The Fifth Circuit reviewed both TXI's and Factory Mutual's methodologies and calculations. The Court then noted the district court's determination that TXI's interpretation was the only reasonable one and adopted its deductible figure. The district court rejected Factory Mutual's methodology finding it rendered superfluous the second sentence of the contractual definition at issue: "The 100% daily Time Element value of the objects will be the full percentage contribution, which would have resulted had the loss or damage not occurred, to the 100% daily Time element value of the entire premises at the location." In short, the district court found it necessary to consider the loss in the context of the total premises. The Fifth Circuit, finding the contract language ambiguous, held that the contract was subject to opposing yet reasonable interpretations. Faced with multiple reasonable interpretations of an insurance contract, the Fifth Circuit noted it need not choose which interpretation was *more* reasonable. Instead, the Court must resolve the uncertainty by adopting the construction that most favors the insured. Thus, the Fifth Circuit adopted TXI's methodology of calculating the policy's deductible under the "15 Day's Value Time Element of the Objects Experiencing the Loss or Damage."

EFFECT OF CORPORATE MERGER ON KEY MAN POLICY BENEFICIARY

Last week, in *Allen v. United of Omaha Life Insurance Company*, 2007 WL 1441007 (Tex. App. – Fort Worth, May 17, 2007), the Fort Worth Court of Appeals addressed the question of: "When a policy's named beneficiary merges with another entity, and the other entity is the 'surviving company,' are the policy proceeds payable to the surviving company?" In *Allen*, Judy Allen was the widow of Fred Allen. In 2001, Fred Allen was the CEO of CreditWatch Services L.P. and the president of CreditWatch Services' general partner, Stoneleigh Financial. CreditWatch Services purchased a "key man" life insurance policy on Fred's life in the amount of $1,000,000 from United of Omaha Life Insurance Company. Fred signed the application in his individual capacity as the proposed insured, and he signed it in his capacity as president of Stoneleigh as the policy's applicant/owner. In the application, Fred designated CreditWatch Services as the policy's sole beneficiary.

Thereafter, in June 2002, CreditWatch Services, L.P. merged with CreditWatch Services, Ltd., an Ohio limited company. The merger agreement and certificate of merger specified that the surviving entity was CreditWatch Services, Ltd. The insurance policy's beneficiary designation was never changed from CreditWatch Services, L.P.

Fred died of natural causes in December 2002. In September 2003, United Omaha issued a check payable to CreditWatch Services for the policy proceeds. Subsequently, in December 2004, Judy Allen sued United, the insurance agent who sold the policy, CreditWatch and various officers of CreditWatch Services. Judy alleged that because the policy's named beneficiary ceased to exist before Fred died and because the named beneficiary had no insurable interest in Fred's life, the policy proceeds should have been payable to Fred's Estate. The trial court rendered summary judgment in favor of the defendants and Judy appealed.

The Fort Worth Court began its analysis by addressing the effect of a merger on the beneficiary designation. Noting that some Texas cases describe a beneficiary's right to receive life insurance proceeds payable at a future but uncertain date as "property" in the nature of an unmatured "chose in action" that matures at the death of the insured, the Court also examined those cases which describe the beneficiary's interest as an expectancy that matures into a vested interest upon the death of the insured. Both "chose in action" expectancies are conveyable interests under Texas law. Thus, the Court determined that regardless of whether CreditWatch Services' interest in Fred's life insurance policy as a "chose in action" or an expectancy, the interest was transferable and the question was whether the merger effectively transferred that interest to CreditWatch Services, Ltd.

Next, the Court examined the express terms of the merger agreement as well as both Texas' and Ohio's law regarding mergers. The Court found that conveyance of "all of the rights, privileges, immunities, powers and purposes, and all of the property, real and personal, causes of action and every other asset of the Merging Partnership . . ." was sufficient to include and incorporate a transfer and conveyance of CreditWatch Services, L.P.'s interest in the key man policy. In doing so, the Court held that, under the express terms of the merger agreement as well as under the relevant Texas and Ohio statutes, all of CreditWatch Services, L.P.'s rights and interests automatically vested in CreditWatch Services, Ltd. without the need for further act or deed. Because CreditWatch Services, L.P.'s rights as beneficiary of Fred's life insurance policy was transferable, those rights also vested in CreditWatch Services, Ltd. without the need for further action.

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